Arvind Polycot Ltd. Vs. Assistant Commissioner of Income-tax

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Court : Gujarat

Decided On : Jul-11-1996

Reported in : (1996)136CTR(Guj)112; [1996]222ITR281(Guj)

Judge : B.C. Patel and; R.R. Jain, JJ.

Acts : Income Tax Act, 1961 - Sections 10, 36(1), 37, 143(1) and 148

Appeal No. : Special Civil Application No. 1366 of 1996

Appellant : Arvind Polycot Ltd.

Respondent : Assistant Commissioner of Income-tax

Advocate for Def. : Shelat, Adv. for; M.R. Bhatt and Co.

Advocate for Pet/Ap. : J.P. Shah, Adv.

Judgement :

B.C. Patel, J.

1. The petitioner, by filing this petition, has prayed for issuance of a writ of certiorari or any other appropriate writ, order or direction, quashing the notice at annexure 'C' issued under section 148 of the Income-tax Act, 1961 (hereinafter referred to as 'the Act'), and all the further proceedings taken in pursuance thereof including the assessment order if passed.

2. The petitioner, a public limited company, submitted its return for the assessment year 1993-94 on December 20, 1993, along with the statement of total income, statement of business income, etc., a copy of which is at annexure 'A' to the petition.

3. The petitioner made a claim of Rs. 1,27,95,596 in respect of interest stating specifically that this interest has been capitalised in the books and that being in respect of capital borrowed, it is allowable under section 36(1)(iii) of the Act, in accordance with the decision of this court in CIT v. Alembic Glass Industries Ltd. : [1976]103ITR715(Guj) . The Assessing Officer, in exercise of the powers under section 143(1)(a) of the Act sent an intimation dated January 27, 1995, accepting the return as it is, without making any adjustments since all the claims were prima facie patently admissible. A copy of the said order is at annexure 'B' to the petition.

4. It appears that notice under section 148 of the Act has been issued on February 14, 1995, in respect of the assessment year 1993-94 stating that income chargeable to tax has escaped assessment and the assessee was called upon to submit the return, vide annexure 'C' to the petition. As notice under section 148 was issued requiring the assessee to file return of income for the assessment year 1993-94, the same was filed, with a request to furnish a copy of the reasons recorded for issuing notice under section 148 of the Act. It appears that the assessee also reminded about furnishing reasons on October 12, 1995, vide annexure 'F'. The request was rejected, vide letter dated October 13, 1995, vide annexure 'G'. Thereafter, this petition was filed before this court and as notice came to be issued, the reasons were furnished in the form of an affidavit.

5. The first reason as indicated in the affidavit for reopening the assessment is that in the course of general enquiries by the Assistant Commissioner of Income-tax, Central Circle-31, Bombay, the assessee informed that it had purchased 1,25,000 shares of Reliance Industries Ltd. worth Rs. 3.27 crores on March 20, 1993. The Assessing Officer verified this information from the return of income filed by the assessee, and found that the investment in Reliance Industries Ltd., had nowhere been mentioned by the assessee in its balance-sheet or in the profit and loss account.

6. The second reason for reopening the assessment was that the assessee had claimed an expenditure of Rs. 1.25 crores being interest on uninstalled machinery as revenue expenditure. As alleged the inquiries conducted during the course of assessment proceedings for the assessment year 1992-93 revealed that this machinery had been purchased for the purpose of a new business which was yet to start and, as such, the assessee could not have claimed the pre-installation interest as a revenue expenditure. The affidavit indicates that this interest should have been capitalised as cost of machinery purchased.

7. Thus, on the aforesaid two grounds, the Assessing Officer thought it proper to reopen the assessment.

8. So far as the first reason for reopening the assessment on the ground of investment in the shares is concerned, it is clear that the investment in the shares of Reliance Industries Ltd. was purported to be made on August 14, 1993, and not on March 20, 1993, as suggested by the Assessing Officer. Thus, it is very clear that the investment was during the assessment year 1994-95 and not during the assessment year 1993-94. In view of this, it is clear that the investment is subsequent to the year of filing of the return and, hence, there is no question of indicating the same in the previous year of return and, hence, the reason is not tenable at all for reopening the assessment. The record indicates that this has happened due to a typographical error.

9. So far as the second reason for reopening of the assessment is concerned. Mr. Shah, learned advocate, has pointed out that there is no new business as indicated in the affidavit of the opponent, and in the absence of such ground, there is no justification in reopening.

10. The assessee is engaged in the manufacturing of cloth. It appears that new air-jet looms were purchased with a view to manufacture fabrics having width of 56 inches. The old machines were capable of producing fabrics having width of 36 inches to 44 inches only. As it was not possible to manufacture fabrics having width of 56 inches with old looms, new air-jet looms were purchased. It appears that this has led the Assessing Officer to believe that the assessee has purchased the machinery for the purpose of new business. It thus appears that modernisation

has been considered by the Assessing Officer as a new business. It is not disputed that the assessee-company, having its manufacturing activity at Ahmedabad, is engaged in weaving and spinning, and manufacturing varieties of textile cloth. It is clear that the business is the same, the administration is the same, the funds are common, the staff is the same, persons in the management are the same and the output would be textile fabrics. Thus, it is clear that it would not be a new business.

11. In the case of CIT v. Prithvi Insurance Co. Ltd. : [1967]63ITR632(SC) , the assessee was carrying on business of life insurance as well as general insurance. Both the businesses were attended to by its branch managers and agents without any distinction. There was one common administrative organisation and administrative expenses and other expenses were incurred from a common fund. In this background, the question was, whether unabsorbed losses incurred by the assessee in the earlier years in respect of the life insurance business could be set off against the profits of the general insurance business of the relevant previous years under section 24(2) of the Indian Income-tax Act, 1922. The apex court held that the assessee was entitled to set off claimed by it as the life insurance business and the general insurance business constituted one composite business. It was held that inter-connection, interlacing, interdependence and unity were furnished by the existence of common management, common business organisation, common administration, common fund and common place of business. The court held that (at page 636) :

'Counsel for the Commissioner contended that life insurance business and general insurance business were separate businesses and he relied in support of that contention primarily upon the method of computation of taxable income of the life insurance business and of the general insurance business. Both in respect of the life insurance business and general insurance business, there are, as already mentioned, special methods of computation of income. But because there are distinct methods of computation of taxable income of the insurance business, and the general provisions of the Income-tax Act relating to computation of profits and gains of a business in section 10 and the related sections are inapplicable, it does not follow that the two businesses cannot be the 'same business' within the

meaning of section 24(2). Whether two or more lines of business may be regarded as the 'same business' or 'different businesses' depends not upon the special methods prescribed by the Income-tax Act for computation of the taxable income, but upon the nature of the businesses, the nature of their organisation, management, source of the capital fund utilised, method of book-keeping and a host of other related circumstances which stamp them as the same or distinct.'

12. In the case of Standard Refinery and Distillery Ltd. v. CIT : [1971]79ITR589(SC) , the assessee-company owned a distillery and had acquired a sugar refinery, obtained on lease a sugar and gur refining company with effect from June 1, 1945. During January 29, 1946, to April 23, 1946, the assessee-company purchased 41,300 shares of that company and sold them, on April 30, 1947, at a loss. After setting off this loss against the income for the assessment year 1948-49, there was a balance of the loss and the question was whether the appellant could carry forward the unabsorbed loss in the sale of the shares and set it off against the income from sugar manufacturing and distillery for the assessment year 1949-50 under section 24(2) of the Act of 1922. The Tribunal found that : (i) there was a single trading and profit and loss account and sales of spirit, sugar and molasses as well as stocks and shares appeared in that account; (ii) the share transaction as well as the business had been dealt with by a common organisation; (iii) the business of the company as well as the transaction in shares were attended to as part and parcel of the business of the appellant; and (iv) a common fund was utilised both for business purposes as well as for the purchase of shares. The apex court held that the share transactions as well as the business of manufacturing sugar and other commodities constituted the same business within the meaning of section 24(2) of the Indian Income-tax Act, 1922, and the appellant was entitled to set off the unabsorbed loss in the sale of shares against the income from sugar manufacturing and distillery for the assessment year 1949-50.

13. Mr. Shah, learned counsel for the petitioner, has pointed out a number of decisions on this line. In the case of CIT v. Alembic Glass Industries Ltd. : [1976]103ITR715(Guj) , the manufacturing units were situated at different places (and that too in two different States). The company had one unit at Baroda which

was engaged in the manufacture of glass. The company established a new unit at Bangalore. In that case, one company alone managed the whole business organisation of both the units and the products of both the units were considered the production of that company itself. The mere fact that there was no common place of business because the Bangalore unit was situated many miles away from the Baroda unit does not matter. In that case the court held that the new factory at Bangalore did not constitute a new business but was only an establishment of a new unit of the existing business at Baroda. Thus, it was held that the interest incurred by the assessee on the borrowing utilised for the purpose of establishing the Bangalore unit is for the purpose of the assessee's business and as such allowable as revenue expenditure.

14. In the case of Bansidhar Pvt. Ltd. v. CIT : [1981]127ITR65(Guj) , the assessee, which was a private limited company, was carrying on different businesses at different points of time, such as purchase and sale of cloth (this business continued up to the year of account and even thereafter), processing of cloth and manufacturing of chemicals and dyes (this business was closed in the year of account), manufacture of machinery (this business was closed on August 1, 1961), and steel plant and rolling mill (this business was closed on September 30, 1961). Upon the closure of one business in the year of account, a total sum of Rs. 9,603 was paid by way of retrenchment compensation. Upon the closure of the other two businesses, i.e., manufacture of machinery and steel plant and rolling mills, the assessee could not recover outstanding dues of Rs. 34,617 and the said amount was written off as bad debt in the year of account. In the assessment, the assessee claimed as a deduction under section 37, the sum of Rs. 9,603 paid as retrenchment compensation and it also claimed as a deduction under section 36(1)(vii), the amount of Rs. 34,617 by way of bad debts. The Income-tax Officer, on appeal, the Appellate Assistant Commissioner and on further appeal, the Income-tax Appellate Tribunal rejected both the claims. The Tribunal held that since retrenchment compensation was paid and bad debts were incurred in businesses totally distinct from the business carried on by the assessee, the deductions could not be allowed in the assessment of the assessee, relying upon the following facts and circumstances :

(i) the several businesses were widely different in nature and they covered both manufacturing and trading activities;

(ii) the different businesses were carried on at different places;

(iii) each business had its own staff including different managers and the staff was not interchangeable.

(iv) inter se transactions between the various businesses were separately and meticulously recorded;

(v) the closure of one business was not shown to have affected the other businesses - in fact, out of five different businesses, three had closed down without affecting the remaining two businesses which were still functioning;

(vi) different books of account were maintained for each business and separate profit and loss account and balance-sheet were prepared in respect of each business although ultimately the accounts were consolidated into a common account;

(vii) the overall control of the board of directors over all the businesses, common ownership of the various businesses, common source of finance, consolidation of accounts and common assessment proceedings in different years were factors of no material importance; and

(viii) even in the case of a limited company, there can be different businesses, although overall control is retained by the same board of directors.

15. Considering various judgments, the Gujarat Court held as under (at page 73 of 127 ITR) :

'In the instant case, the board of directors of the assessee, which is a private limited company, was in overall control of all the five business activities which were owned and carried on by the assessee. There was a common fund from which the necessary capital and working funds were supplied to the various business activities. The ultimate gain or loss of business was also worked out by a consolidated profit and loss account and balance-sheet. The source of finance for

running the various businesses was thus one and single and there was a consolidation of accounts for the purpose of ascertaining the ultimate working result of the business carried on by the assessee. Merely because there was a separate staff, which was not inter-transferable, the unity of control was not affected since, at the apex, there was a common management and administration in view of the overall control of the various businesses vesting in the board of directors of the assessee-company. Though some or most of the businesses were carried on at different places, the ultimate control was exercised at the registered office of the assessee-company and that circumstance also, therefore, did not detract from the unity of control.'

16. Mr. Shah, learned counsel pointed out that the decision of the apex court in the case of Veecumsees v. CIT : [1996]220ITR185(SC) , wherein the assessee who was doing jewellery business also commenced business of cinematographic films. The theatre was built in 1962 and was run by the assessee until July 31, 1965, when it was transferred to another firm. For the years during which the assessee exhibited films in the said theatre, the interest paid on the loans obtained for constructing it were allowed by the Revenue as a deduction under section 36(1)(iii) of the Act of 1961. The Income-tax Officer declined the deduction for the assessment years 1967-68, 1968-69 and 1969-70 on the ground that the business of exhibition of firms in the said theatre was no longer in existence. The Appellate Assistant Commissioner allowed the deduction. The Tribunal found that there was no dispute that for the construction of theatre, the assessee has made heavy borrowings and the interest on such borrowings has been allowed by the Revenue as a deduction as the assessee was running the said theatre as its own business; that the assessee had admittedly paid the interest in question for the years under appeal in respect of the loans obtained for the purpose of investing in the business of exhibition of films. The Tribunal also found that the business carried on by the assessee was as jeweller and the running of the said theatre, restaurant, etc., were composite; that the assessee was carrying on the business in jewellery as well as the exhibition of films till July 31, 1965, and that only thereafter the activity of exhibition of films discontinued; and that the liability to pay interest had arisen in respect of the business carried on by the assessee till July 31, 1965. The Tribunal, accordingly, upheld the decision of the Appellate Assistant Commissioner to

permit the deduction under section 36(1)(iii). The High Court came to the conclusion that since the closing of the cinema business had not affected in the least the assessee's business in jewellery, there was no inter-connection, inter-lacing or inter-dependence between the jewellery business and the cinema business. The High Court disallowed the deduction. The matter was carried to the apex court and the apex court held that (at page 189) :

'The fact that the Revenue had during the years when the assessee carried on the business of cinematographic films permitted as a deduction under section 36(1)(iii), the interest on loans obtained by the assessee for the purpose of constructing the said theatre shows that at time when the loans were obtained the said theatre was a part of the business of the assessee. It was interest on these loans, borrowed for the purpose of the business of the assessee, which was being paid in the years in question and the Tribunal was, in our view, right in concluding that such interest had to be treated as a deduction under section 36(1)(iii). The loans had been obtained for the purposes of the assessee's business. The fact that the particular part of the business for which the loans had been obtained had been transferred or closed down did not alter the fact that the loans had, when obtained, been for the purpose of the assessee's business. The test of 'same business' appropriate for set-off of carry forward losses is not appropriate here.'

17. Thus, it is clear that what is required to be seen is whether business is carried on by the assessee or not. In the instant case, we put a question to Mr. Shelat, learned counsel that if the assessee is engaged in the running of railways and if meter gauge lines are converted into broad gauge lines, would the assessee not be entitled to the benefit of section 36(1)(iii), to which Mr. Shelat stated in view of the aforesaid decision, he need not be questioned. Suffice it to say that the assessee was manufacturing cloth of a particular width and if machinery is purchased for the purpose of manufacturing cloth having larger width, it cannot be said that it is a new business.

18. Learned counsel for the Revenue contended that this court should not interfere in a matter like this at this stage because only a notice is issued and it is open for the assessee to appear before the authority in response to the notice. As against

this, Mr. Shah vehemently submitted by pointing out that the officer is acting without jurisdiction and it is the duty of this court to interfere. He had drawn our attention to the decision of the apex court in the case of Calcutta Discount Co. Ltd. v. ITO : [1961]41ITR191(SC) , which reads as under :

'.... though the writ of prohibition or certiorari would not issue against an executive authority, the High Courts had power to issue in a fit case an order prohibiting an executive authority from acting without jurisdiction. Where such action of an executive authority acting without jurisdiction subjected, or was likely to subject, a person to lengthy proceedings and unnecessary harassment, the High Courts would issue appropriate orders or directions to prevent such consequences. The existence of such alternative remedies as appeals and reference to the High Court was not, however, always a sufficient reason for refusing a party quick relief by a writ or order prohibiting an authority acting without jurisdiction from continuing such action. When the Constitution conferred on the High Courts the power to give relief it became the duty of the courts to give such relief in fir cases and the courts would be failing to perform their duty if relief were refused without adequate reasons.'

19. In view of this, the contention raised by the Revenue on this issue is required to be rejected.

20. In the result, this application is allowed. Order at annexure 'C' is quashed and set aside.

21. Rule made absolute accordingly. No order as to costs.